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Increasing Enforceability of Mandatory Arbitration Clauses in Wills and Trusts

Can a testator or settlor require parties to submit disputes to alternative dispute resolution?

By Steven K. Mignogna

A hot issue percolating among the states is whether a clause in a will or trust requiring alternative dispute resolution — usually arbitration — should be enforced by the courts. While initially courts appeared to frown on such provisions, the trend has shifted recently, particularly with a ruling by the Texas Supreme Court upholding such a clause.

For a number of years, drafters have searched for ways to eliminate, or at least curtail, court proceedings as to estates and trusts, in the planning stage. Indeed, some websites contain sample standards and clauses. For instance, the American Arbitration Association website not only has rules for the arbitration of estate and trust disputes, but clauses to use in an effort to direct the parties to alternative dispute resolution.

The need for mediation and arbitration in estate and trust disputes is increasing. See generally, Steven K. Mignogna, "Mediation on the Rise: As Estate Disputes Increase, the Use of Mediation and Arbitration Will Become More Frequent," 187 *N.J.L.J.* 416 (2007). As this demand has increased, the debate among lawyers, commentators, judges and scholars has escalated as to whether a testator or settlor can actually *require* the beneficiaries or fiduciaries to submit disputes to alternative dispute resolution. The arguments in favor of enforcing such provisions generally parallel the benefits of arbitration and mediation — i.e., saving time and money, managing emotions and relationships (particularly pertinent in family estate or trust disputes) and maintaining privacy. See Stephen Wills Murphy, "Enforceable Arbitration Clauses in Wills and Trusts: A Critique," 26 Ohio St. J. on Disp. Resol. 627, 635-36 (2011).

On the other hand, traditionally, the parties to litigation agree to submit their fight to alternative dispute resolution, usually either in their underlying contract or once the dispute has arisen. By the nature of trusts and estates, however, this mutuality of consent does not occur. Some argue that the beneficiary has in effect accepted or agreed to the terms of the bequest, but, in the real world, few beneficiaries will renounce a bequest due to those conditions. Our country also has a long tradition of the courts exercising unique powers over wills and trusts, and the fiduciary duties owed by executors and trustees. This jurisdiction encompasses a variety of unique elements, such as judicial accountings or actions by fiduciaries for advice and instruction. See generally S. I. Strong, "Arbitration of Trust Disputes: Two Bodies of Law Collide," 45 Vand. J. Transnat'l. L. 1157 (2012).

In the end, "most commentators and a growing number of courts and legislatures appear to adopt the view that mandatory arbitration clauses located in trusts are enforceable, despite a few well-publicized judicial decisions to the contrary." S. I. Strong, "Empowering Settlors: How Proper Language Can Increase the Enforceability of a Mandatory Arbitration Provision in a Trust," 47 Real Prop. Tr. & Est. L. J. 275, 280 (2012). Indeed, certain states (e.g., Arizona and Florida) have enacted

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statutes delineating situations in which a provision in a will or trust requiring arbitration would be enforceable.

Against the backdrop of these competing arguments and policies, on May 3, the Supreme Court of Texas sided with the enforceability of these provisions, in *Rachal v. Reitz*, No. 11-0708, 2013 Tex. LEXIS 348 (Tex. May 3, 2013).

Andrew Francis Reitz established the A.F. Reitz Trust in 2000, naming his sons, James and John, as sole beneficiaries and himself as trustee. The trust included an arbitration provision specifying Andrew's intent that any dispute involving the trust be resolved by arbitration as the sole and exclusive remedy. Upon Andrew's death, Hal Rachal Jr., the attorney who drafted the trust, became the successor trustee.

In 2009, John Reitz sued Rachal for allegedly misappropriating trust assets and failing to provide an accounting to the beneficiaries. John Reitz sought Rachal's removal as trustee, a temporary injunction and damages.

Rachal moved to compel arbitration pursuant to the arbitration clause in the trust. His request was denied by both the trial court and the court of appeals. The court of appeals held that to be binding, an arbitration provision must be the product of an enforceable contract between the parties. The trust, the court concluded, was not a contract due to the absence of consideration and the unilateral nature of the trust's terms. The appeals court concluded that the question of whether a trust's arbitration provision can be enforced was ultimately an issue for the legislature to resolve.

The Texas Supreme Court reversed, finding that under the Texas Arbitration Act (TAA) an arbitration provision in an inter vivos trust is enforceable against the beneficiaries. The court first found that the settlor's intent, divined from the four corners of the trust, unequivocally indicated that arbitration was to be the sole and exclusive remedy for any disputes to arise from the trust.

The Texas Supreme Court emphasized that in drafting the TAA, the legislature specifically chose to enforce "agreements" to arbitrate rather than limiting valid arbitration provision to contracts. The court reasoned that an agreement posed a lower threshold than a contract, requiring only "mutual assent" of the parties. Therefore, if there was mutual assent between the parties, then the trust was an agreement and the arbitration provision was valid.

The court built the framework to find mutual assent by discussing a case where a nonsignatory to a contract attempted to seek the benefits of a contract and was precluded from simultaneously avoiding the burdens under the contract. The court then noted it had previously adopted the federal doctrine of benefits estoppel, which holds that a nonsignatory party may not avoid the burdens of a contract when he has consistently attempted to enforce the beneficial provisions of the same contract.

The court determined that direct benefits estoppel applies to arbitration provisions in trusts because a beneficiary may opt out of the trust to show that he does not consent to its terms. By attempting to enforce the advantageous terms of the trust, the beneficiary manifests his assent to all terms, including the arbitration provision. The court concluded that because John Reitz was suing to enforce the trust provisions against the trustee, he had therefore manifested his assent to the terms of the trust, including the arbitration provision.

Finally, the Texas Supreme Court distinguished Texas from other jurisdictions that had decided that arbitration provisions in trusts are unenforceable. It noted that unlike the Arizona arbitration statute, which required the provision to appear "in a written contract," the TAA expressly provided for arbitrations in "agreements." The court concluded that Rachal had met his burden of proving the arbitration provision was valid in the agreement, and Reitz had manifested his assent to that provision in the agreement by seeking to enforce terms of the contract against Rachal.

It remains unclear whether the trend will change as the enforceability of these clauses continues to be debated. In any event, those professionals who deal with estates and trusts need to be aware of these developments, and certainly should eradicate any outmoded notion that these clauses are never to be enforced. ■